
SECTION: CORE Holding Company Examination Program Section 730

Program Guidance: This CORE Holding Company Program should be used to examine high risk or complex holding company enterprises. Also, be sure to consider the unique characteristics of the specialized holding company structures discussed in Section 900. This Program may also be used to supplement the Abbreviated Holding Company Examination Program (Section 720). You should complete only those sections of the program that the EIC deems necessary to evaluate each CORE examination area and to support the overall examination conclusions.

C – Capital

Examination Objectives

Determine the holding company's financial resources and assess its current and prospective effect on the subsidiary thrift.

Evaluate the holding company's level of debt and capital structure.

Examination Procedures

Wkp. Ref.

1. Assess the holding company's ability to service its outstanding debt and the degree the thrift is relied upon to upstream funds to service the debt. Determine whether double leveraging is occurring, and to what extent.
 - Determine if the level of consolidated debt is increasing and if interest expense is a significant portion of recurring income.
 - Calculate the ratio of ***consolidated holding company debt to consolidated tangible capital***. (For holding companies with significant nonthrift operations, particularly in industries with large investments in fixed assets, calculate the ***debt-to-total asset*** ratio.)
 - Calculate the holding company's ***leverage*** ratio.
 - Compute the ***debt-to-equity*** ratio on a market value and book value basis to assess the market perception of the company.
 - Consider if the holding company is investing in leveraged instruments such as futures and options that can require volatile cash needs.
 - Determine to what degree the holding company has retained recourse (explicit or implicit) related to off-balance sheet funding activities such as asset securitizations.

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

- Consider whether the holding company is committed to investments with material cash needs, such as major construction projects and other capital intensive business activities.

[Click&type]

[Click&type]

2. Assess the holding company’s consolidated capital structure. Consider the quantity and composition of capital. Does the holding company have enough capital to adequately protect the subsidiary thrift from risky activities or adverse events within the holding company enterprise? Consider the overall risk profile and all risk factors, including credit, market, operational, and legal risks.
- Determine if the holding company’s capital position has deteriorated since the last examination. If so, cite the reasons.
 - Analyze whether the holding company has significantly restructured its as- set/liability portfolio or made significant acquisitions or divestitures.
 - Review the composition of consolidated capital. How would capital be affected if thrift capital conventions, bank holding company capital conventions, or the capital conventions of other functional regulators are applied?
 - Consider the extent to which the holding company uses debt-like instruments such as trust preferred stock for financing. Determine if management developed a sound plan for investing the proceeds of any such financing activities. Determine how interest or dividend obligations are financed, specifically, if the thrift is relied upon, in whole or in part, to service such obligations?
 - Review the holding company’s capital plans. Consider the effect of future transactions and major acquisitions on capital. Assess the holding company’s access to capital markets.
 - In cases where capital is considered inadequate, discuss with management any plans to access the capital markets or otherwise augment capital.

[Click&type]

[Click&type]

3. Consider the effect of the company’s dividend practices on its capital condition.
- Identify situations where the company or thrift must borrow funds or sell assets to maintain dividend payments.
 - Calculate the holding company’s *dividend payout to earnings* ratio and determine if it is consistent with the business plan.

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

- Compare the dividend payout ratios, net income, and asset size of significant affiliates to assess relative contributions.

[Click&type]

[Click&type]

4. For affiliates that are regulated by another state or federal agency, determine if there are any agreements or conditions imposed that would require the holding company to devote financial resources (such as capital contributions) to that entity. If such an agreement exists, determine the extent to which it could ultimately have an adverse impact on the subsidiary thrift.

[Click&type]

[Click&type]

O – Organizational Structure

Examination Objectives

Analyze ownership and control.

Determine if there is evidence that the holding company structure is designed to circumvent OTS policies.

Identify activities of the holding company and its noninsured subsidiaries to determine permissibility.

Assess what risks the activities of the holding company and its other affiliates pose to the thrift.

Examination Procedures

5. Analyze changes in the holding company enterprise since acquisition or the previous examination.

Compare the current organization chart with one at the time of acquisition or the previous examination.

- Review organizational data provided by any other regulatory agency.
- Identify all tiers of the holding company. Ensure that the OTS holding company database accurately reflects the current structure.

Exam Date: _____

Prepared By: _____

Reviewed By: _____

Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

- Determine if the holding company has acquired, formed, divested, or transferred any subsidiaries or significant portion of its consolidated assets.

[Click&type]

[Click&type]

6. Determine whether any individual or entity - directly, indirectly, or by acting in concert - has acquired control.

- Review a list of all significant shareholders to determine the number of shares owned and percentage of outstanding stock held. (Significant stockholders include any person or entity that owns ten percent or more of stock either individually or acting in concert.)
- Determine whether any changes in ownership have occurred since acquisition or previous examination.
- Determine whether the holding company repurchased a significant amount of its stock or if any new issuances of capital stock, capital notes, or subordinated debentures occurred.
- Consider exemptions contained in Section 10(a) of the Home Owners' Loan Act and 12 CFR Section 574.3.

[Click&type]

[Click&type]

7. Review the activities of the holding company and other affiliates.

- Evaluate the risk that the activities of the holding company or other affiliates pose to the thrift.
- Ensure that the holding company is not engaged in any acts or acquisitions prohibited by 12 CFR 584.4 or 584.9 regarding ownership interests in nonaffiliated companies or control of mutual thrifts, respectively.

[Click&type]

[Click&type]

R – Relationship

Examination Objectives

Assess the influence of the board of directors and management on the thrift.

Consider how integrated the thrift is in the holding company enterprise.

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

Consider the independence of the boards of directors of the thrift, holding company and other affiliates.

Determine if intercompany and insider transactions are appropriate.

Examination Procedures

8. Assess the influence of the board of directors and management on the thrift. Consider the independence of the boards of directors of the thrift, holding company, and other affiliates. Determine whether any of the relationships appear to create a conflict of interest or usurpation of corporate opportunity.

- Identify the principal decision makers of the holding company, including major shareholders. Does the holding company share common officers with the thrift? If so, expand your review in the thrift examination to ensure they are fulfilling their fiduciary role to the thrift.
- Does the holding company have policies and procedures regarding conflicts of interest and intercompany and insider transactions. Evaluate whether such policies are adequate to protect the interests of the thrift and are being followed.
- Determine the thrift's line of reporting to the holding company.

[Click&type]

[Click&type]

9. Review management's written strategic goals and objectives. Evaluate whether the organization's goals have changed, and, if so, assess how they affect the risk-profile and financial condition of the company.

[Click&type]

[Click&type]

10. Assess the adequacy of internal controls, books, records and systems to ensure that the thrift maintains separate corporate identity.

- Determine whether the financial statements are complete, consistent, and accurate. Consider the materiality of the thrift to the overall corporate structure and the scope of the independent audit. Resolve any discrepancies.

Functionally Regulated-Determine if any discrepancies are due to different forms of regulatory accounting practices.

- Identify who performs the audit of the holding company and the thrift and whether there has been a change in auditing firms and the reason for such change.
- Identify who performs the internal audit work for the holding company and determine whether independence requirements have been met.

Exam Date: _____

Prepared By: _____

Reviewed By: _____

Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

- Determine the effect of accounting changes to the financial recordkeeping and reporting processes.
- Review the audit committee minutes and any correspondence between the holding company and the independent auditor to identify financial recordkeeping deficiencies disclosed to the directors.
- Identify any recommendations, criticisms, or comments related to financial recordkeeping and reporting in the most recent independent audit report and prior examination reports of OTS and any other regulatory agency.

[Click&type]

[Click&type]

11. Determine the extent to which the operations of the thrift are integrated with the holding company and other affiliates.

- Assess the risk posed by integrated systems, common risk management practices, central decision making, joint marketing and delivery systems, linked market reputation, size of the thrift in relation to the holding company, and common controls.
- Assess the risk posed by the thrift’s public identity being linked with the holding company. In particular, review the Management Representation letter, or an attached attorney’s letter, to the external auditor detailing pending or threatened litigation that could harm the holding company, and pose reputational risks for the thrift.
- Evaluate whether the thrift can be insulated from adverse events within the holding company structure and carved out as a stand-alone operating entity, if necessary. Ensure that separate corporate identity is maintained.
- Review policies and procedures concerning the operation of the association.
- Review any plans for the thrift.

[Click&type]

[Click&type]

12. Identify and assess the direct and indirect impact on the thrift of any significant inter-company or insider transactions such as loans, guarantees, asset purchases/sales or service contracts. If the transaction is with the thrift, ensure that it is properly reflected in the thrift’s books and records and reviewed for compliance with the affiliate transaction regulations (12 CFR 563.41 and 563.42).

[Click&type]

[Click&type]

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

13. Analyze the tax-sharing agreement and policies, tax payments paid by the thrift to the holding company, and the income tax accounting and settlement practices where the thrift does not file a separate tax return.
- Determine whether the agreement conforms to the OTS policy, particularly with regard to timing, amount, refunds, and treatment of deferred taxes.
 - Determine whether the agreement is governing the current practices of the consolidated group.
 - Determine that taxes collected by the parent holding company from the thrift are not in excess of the amount that the thrift would have paid if it had filed a separate return.
 - Determine that tax payments made by the thrift do not significantly precede the time that a consolidated estimated tax liability would be due and payable by the holding company to the taxing authorities.
 - Determine that the amount and timing of payment of taxes and receipt of refunds by the thrift is no less favorable to the thrift than if it had filed separate returns or made separate estimated payments to the taxing authority.
 - Determine that the deferred tax accounts of the thrift are maintained on its own books and are not transferred to the books of the holding company.
 - Determine if the Internal Revenue Service (IRS) or other taxing authorities have assessed any additional tax payments on the consolidated group.
 - Determine that the holding company has allocated any such additional assessments in accordance with the tax-sharing agreement.
 - If there is a conflict between the tax sharing policies of OTS and the policies of another regulatory agency, contact regional management.
 - Analyze the income tax accounting and settlement practices where the thrift does not file a separate tax return.
 - Review consolidating schedules supporting financial reporting and determine the reasonableness of income tax expense (benefit) to the thrift compared with other members of the group. Timing differences between book income and taxable income may affect the analysis.
 - Determine if any IRS examinations are ongoing and whether any material additional tax obligations are anticipated as a result.
 - Determine if there are outstanding refunds from amended or net operating loss carrybacks that should be allocated to the thrift, or filings of questionable

Exam Date: _____

Prepared By: _____

Reviewed By: _____

Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

recoverability (from the holding company) that could result in chargebacks to the thrift.

[Click&type]

[Click&type]

14. Verify compliance with statutory and regulatory requirements.

[Click&type]

[Click&type]

E – Earnings

Examination Objectives

Assess the trends of the holding company’s earnings and cash flows.

Determine if the holding company’s earnings and cash flow trends may lead it to require the thrift to provide funds through dividends or other means.

Examination Procedures

15. Review the holding company’s financial statements, consolidated audit, management representation letter, and SEC filings. Identify financial trends, discussions of significant accounting practices and any material weaknesses identified in the most recent independent audit report, prior examination reports of OTS or any other regulator.

[Click&type]

[Click&type]

16. Determine the relative strength of subsidiaries to holding company profitability and balance sheet strength.

- Calculate the following ratios to identify financial trends: cash position, current ratio, operating cash flow, debt ratio and return on equity.
- Using trend and peer analysis, evaluate the earnings of the company’s nonthrift operations/subsidiaries over the prior three years and determine the causes for weak or deteriorating performance.
- Evaluate the quality of earnings. Determine whether the sources of earnings of pre-tax income are recurring.
- Assess whether the holding company is in a highly cyclical business.

[Click&type]

[Click&type]

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

SECTION: CORE Holding Company Examination Program Section 730

Wkp. Ref.

17. Use external information to evaluate holding company's financial condition.

- Identify any changes to the bond ratings of the holding company or significant affiliates. Assess the causes for any changes.
- Determine stock price. Compute the *market value to book value ratio* and *price/earnings ratio*. Compare results to the company's peers.

[Click&type]

[Click&type]

18. Analyze the holding company's cash flow.

- Compare the holding company's parent only cash flow from operating and investing activities to the amount provided by the thrift through dividends.
- Determine whether financial flexibility exists from nonthrift sources that would enable the holding company to service its short-term obligations.
- Quantify the amount of cash flow provided to the holding company by the thrift and determine what the company's cash flow position would be without funds from the thrift.
- Compare the amount of interest expense on the parent only borrowings to the amount of dividends received from the thrift.
- Compute the *fixed charge coverage ratio* to determine whether the holding company can meet its contractual obligations from current earnings.
- For those companies unable to fully meet cash flow needs from internal resources, identify the cause and level of the deficit and assess the three year trend.
- In cases of worsening or deficit cash flow positions, obtain or prepare a maturity schedule comparing the levels of resources available to funding requirements over the short term (up to 90 days), intermediate term (91 days to 1 year), and long term (over 1 year).

[Click&type]

[Click&type]

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____